Enhancing knowledge of EU green finance policies in insurance and business valuation

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Intensive Course
Green Finance & Sustainability

Insurance of Catastrophic Losses

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Insurance of Catastrophic losses

What types of risks does insurance cover?

- *There must be a sufficiently large number of similar and independent exposure units;*
- *The loss must be accidental and unintentional;*
- *The loss should be definite and measurable;*
- *The loss should not be catastrophic;*
- *The chance of loss must be calculable;*
- *The premium must be economically feasible*

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Insurance of Catastrophic losses

The natural **disaster risk does not fully meet** the following requirements:

- When a natural disaster takes place, often it is very difficult to measure the amount of loss, or at least the actual loss can be measured only after a certain period of time.
- As the “catastrophe” is the synonym of disaster, the loss resulted from the natural disasters is catastrophic.
- The natural disasters occur in irregular basis, therefore their probability cannot be accurately estimated. As a result the natural disaster risk does not fully satisfy the requirements of an insurable risk.

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Insurance of Catastrophic losses

Insurers cover catastrophic losses through:

•*Reinsuring their activity – shifting a part or the whole risk written from one insurer to another insurer (reinsurer).*

•*Dispersing their coverage over a large area – assuming different types of risk.*

•*Financial markets - issuing financial instruments, contingent surplus notes, catastrophe bonds and exchange traded options.*

•*Microinsurance* - providing insurance against natural disasters to poor individualsmers.

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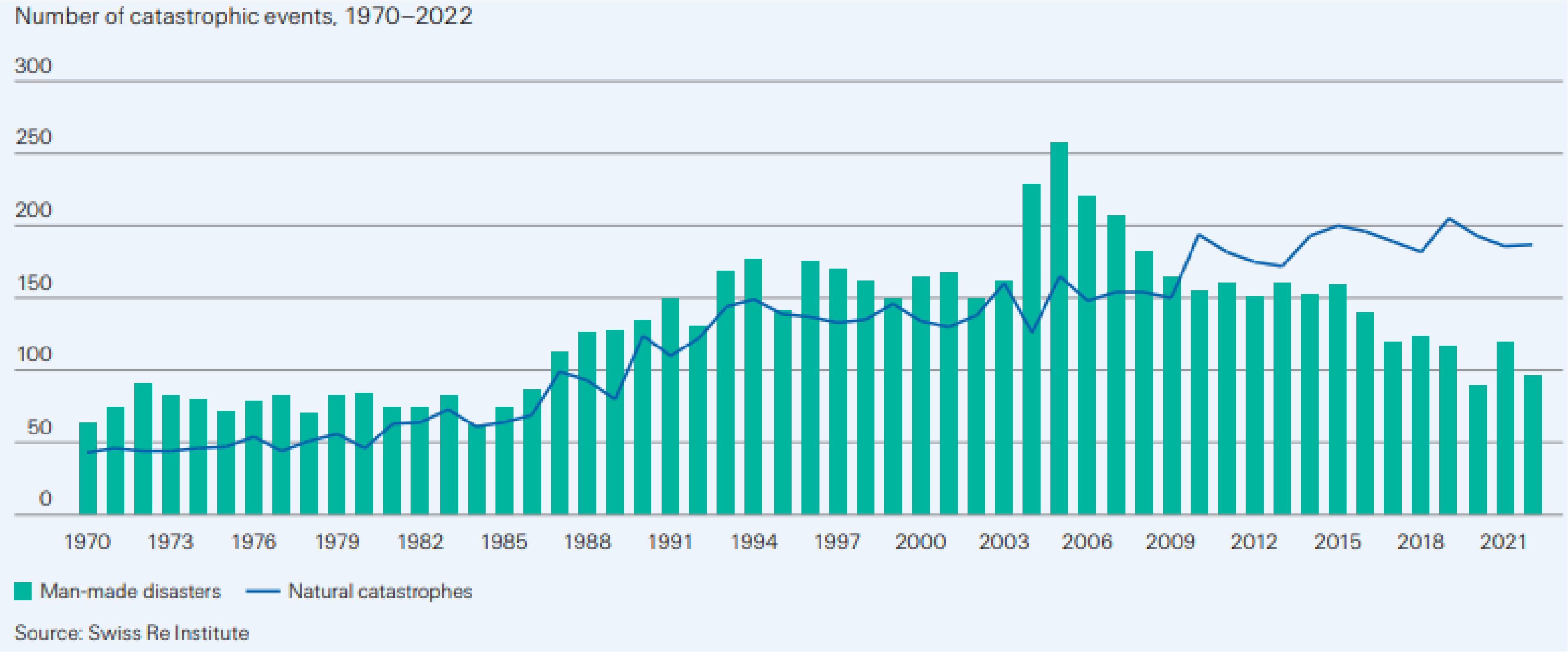
Insurance of Catastrophic losses



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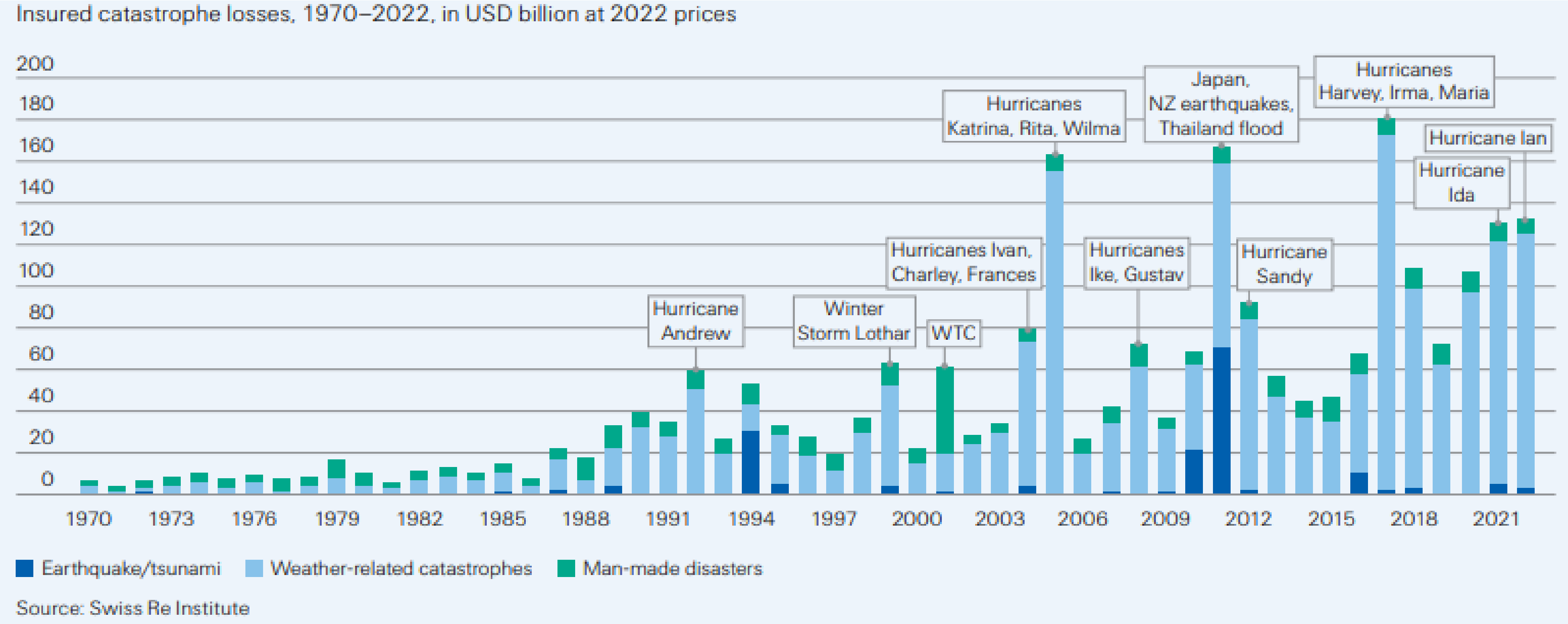
Insurance of Catastrophic losses



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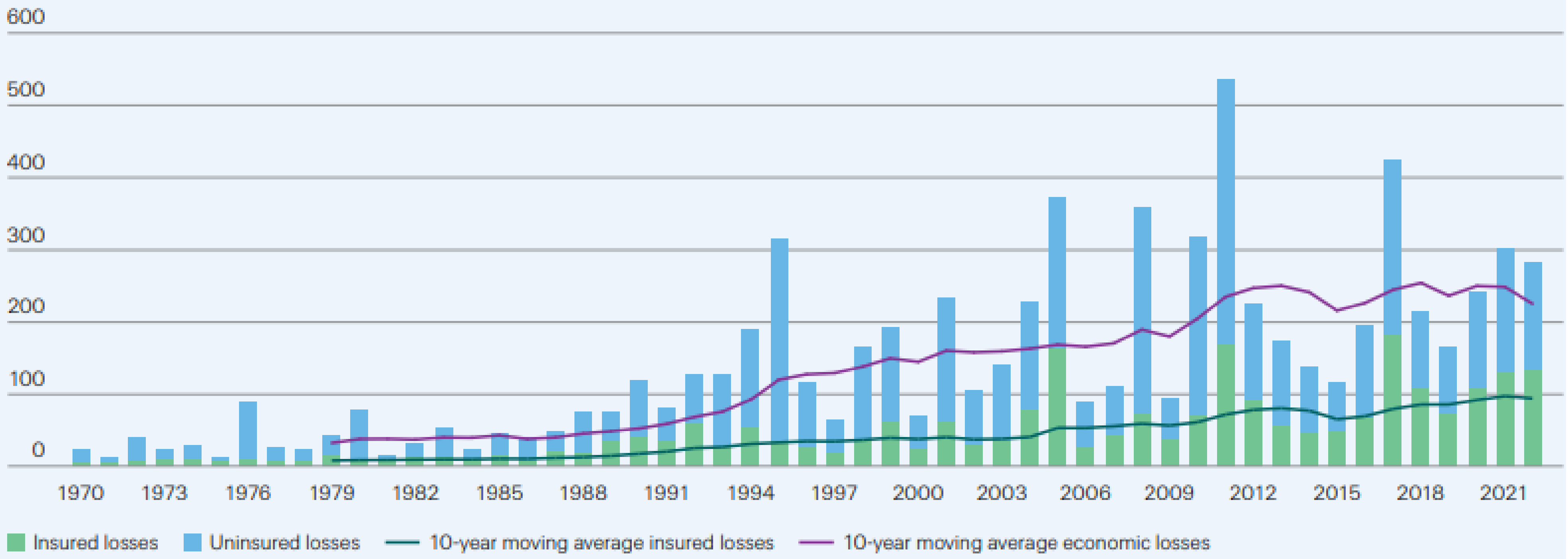
Insurance of Catastrophic losses

Insured vs uninsured losses, 1970 – 2022, in USD billion at 2022 prices



Economic losses = insured + uninsured losses. Source: Swiss Re Institute

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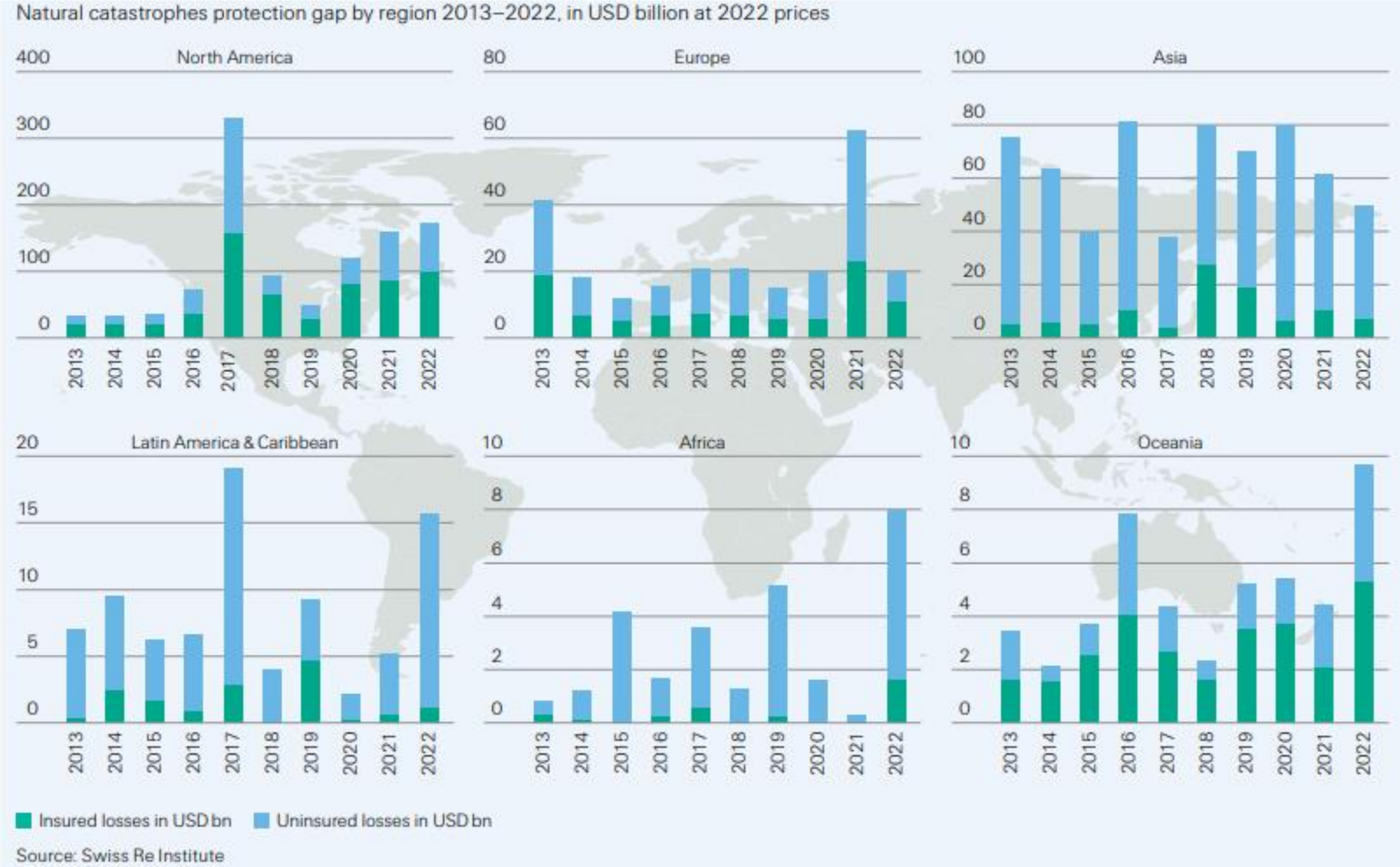
Insurance of Catastrophic losses



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Insurance of Catastrophic losses

In Mongolia herders can purchase an index-based insurance policy to protect them against livestock losses due to conditions of extreme winter weather. The insurance program is a combination of self-insurance, market-based insurance and social safety net. Small losses which do not affect their viability are retained by the herders, while larger losses are transferred to the private insurance industry. Only the final layer of catastrophic losses is borne by the government.

In France, private insurers are required to offer catastrophe insurance in all-hazards property policy. Policies are not risk based and the program is reinsured through a public administered fund. If the fund does not satisfy the claims, taxpayers will be called to pay.

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Insurance of Catastrophic losses

According to the Turkish Catastrophe Insurance Pool launched in 2000, earthquake insurance policies are obligatory for all property owners in Instanbul and other high-risk urban centers. Apartment owners pay a premium based partly on their risk to a privately administered public fund. If the fund cannot meet claims after a major earthquake, the World Bank provides a contingent loan .to the pool.

The Mexican government has chosen to insure its catastrophe reserve fund, FONDEN, against earthquakes with a mix of reinsurance and a catastrophe bond. In 2006, FONDEN issued a USD 160 million catastrophe bond (CATMEX) to transfere Mexico’s earthquake risk to the international capital markets. It was the first country that issue a multi-peril multi-region cat bond using the World Bank’s Multicat Program.

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The Caribbean Catastrophe Risk Insurance Facility (CCRIF) went into operation in June 2007 with the participation of 16 Caribbean countries. The Caribbean Island States have formed the world's first multi-country catastrophe insurance pool, reinsured in capital markets, to provide governments with immediate liquidity in case of large losses due to hurricanes and earthquakes.

In Romania, in 2008, the Pool Against Natural Catastrophes (PAID) was set up as an insurance reinsurance company, formed by the association of 12 insurance companies. The insurers which are members of Catastrophe Insurance Pool, sell mandatory indemnity-based insurance against earthquakes, floods and landslides.

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Insurance of Catastrophic losses

According to the World Bank suggestions (draft law of 2014) – the involvement of insurance market in managing disaster losses ***should be obligatory*** *(following Romanian experience) and a draft law was prepared by AFSA .*

In 2023, a second draft law (based on Turkish, Romanian and Philippine experience) - foresees the creation of the National Earthquake Fund, which will be financed mainly from the premiums collected by the public, but also receives financing from the state budget or various donations. The fund will be managed by an Agency for Compulsory Earthquake Insurance, where the Ministry of Finance will represent the government share.

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Thank you for your attention

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